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TAGS: ECON PGOV PINR PREL CU  
SUBJECT: INTERPRETING CUBA'S 2008 ECONOMIC PERFORMANCE

REF: A. HAVANA 969  
1B. HAVANA 752

Classified By: COM Jonathan Farrar for reasons 1.4 (b) and (d)

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SUMMARY  
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11. (SBU) On January 7, the Cuban Office of National Statistics published a Panorama of Economic and Social Indicators for 2008 providing some detail behind the data reported to the National Assembly (ref A) by Raul Castro and his economic team December 26-27. While the availability of statistics in Cuba has noticeably improved over the past two years, interpreting their true significance remains a challenge. GDP, as uniquely measured in Cuba, grew by a disappointing 4.3 percent led by service exports, transportation, and tourism. In addition to three hurricanes, Cuba experienced a perfect storm in its current account with the price of its key imports (food and fuels) rising and the price of its key exports (nickel and, to a much lesser extent, sugar) falling. As a result, the trade deficit in goods increased by over USD 4 billion or 68 percent from 2007. For the same reasons, the fiscal deficit also took a hit, climbing 31 percent in 2008 to 6.7 percent of GDP (septel). Raul's theoretical solutions of reducing some subsidies (most likely the ration card) and raising wages are much more likely to improve the Cuban economy, if one day implemented, than his more specific and immediate prescriptions of limiting travel and perks for government officials. End Summary

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HOW CUBAN GDP GROWS  
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12. (SBU) At Fidel Castro's urging, the Government of Cuba (GOC) started using an unconventional method for calculating GDP in 2003. Rather than calculating the domestic value of government services provided for free (healthcare, education, etc.), the GOC values these services at prices that would have been charged in an unspecified market economy. Furthermore, some GOC official statistics (e.g. GDP and the state budget) combine Cuba's two currencies, the Cuban non-convertible peso (CUP) and Cuban convertible peso (CUC), at the official exchange rate of 1 to 1 rather than the unofficial but formally traded

exchange rate of 24 to 1. Thus, the absolute value for GDP reported in official statistics is meaningless and should not be compared with other countries. However, changes in GDP year to year remain meaningful under the assumption that the GOC has not made any additional, unreported changes in methodology.

¶ 13. (SBU) Raul Castro and his economic team reported 4.3 percent real GDP growth in 2008, well below the 8 percent originally projected, the 7.3 percent reported for 2007, and the 12.1 percent reported for 2006. The reasons cited for the disappointing growth include the U.S. embargo, the devastating hurricane season, higher prices for fuels and food imports, and lower prices for key exports (nickel). These excuses are only partially valid. It's hard to imagine that the GOC'S projection of 8 percent growth for 2008 did not already take into account the likelihood that U.S. sanctions would continue throughout the year. While the three hurricanes in August and September significantly impacted economic activity in the second half of the year, the GOC had already warned that GDP growth for the first half of 2008 was slower than expected at 6 percent.

¶ 14. (U) The GOC attributed more than 85 percent of Cuba's 4.3 percent GDP growth in 2008 to just four sectors: public health and social assistance (41 percent); transport, storage, and communications (16.2 percent); import duties (15.2 percent); and hotels and restaurants (13.9 percent). It is likely that the public health and social assistance sector includes inflated domestic spending figures using the GOC's unique methodology plus income earned (in cash and goods) from exporting medical services, primarily to Venezuela. The GOC focused government spending on improving transportation of goods and people with highly publicized purchases from China, Russia, Vietnam, and Iran.

¶ 15. (SBU) In a more conventional breakdown, Economy and Planning Minister Jose Luis Rodriguez reported on December 27 that personal consumption represents 49 percent of GDP (down from 53 percent in 2007), social (government) consumption represents 29 percent (up from 28 percent), investment represents 14 percent (same as 2007), and net exports represent 8 percent (up from 5 percent). The increase in net exports as a percentage of GDP is surprising considering the deficit in the trade of goods grew by 68 percent to nearly USD 11 billion. As a result, we can assume that the surplus in the trade of services grew even faster, although the GOC offers very little transparency into this figure which likely includes exports of medical services (doctors, nurses), tourism, and other consultancies.

¶ 16. (U) Planning and Economy Minister Rodriguez estimates 2009 GDP growth of 6 percent, but, unlike previous years, provided no detail into how Cuba will achieve it.

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MORE TRADE AND TOURISM  
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¶ 17. (SBU) Cuba has a relatively open economy in the sense that it is heavily dependent on the external market, in particular trade, tourism, and remittances. Total trade in goods increased 33 percent in 2008, dominated by a 44 percent increase in imports. Cuba reportedly spent USD 907 million more on food and USD 1.336 million more on fuels, representing half of the USD 4.3 billion increase in the trade deficit. (NOTE: Through November, imports from the United States were already 50 percent higher than 2007. U.S. exporters value the sales at USD 660 million, but the cost to Cuba is closer to USD 800 million. END NOTE) Cuba also increased purchases of machinery and equipment, most likely related to the transport, construction, and communications sector post-hurricanes.

¶ 18. (C) According to official statistics, exports somehow managed to increase by 2.1 percent even though the average

price of Cuba's most important export, nickel, dropped 41 percent and the tonnage produced dropped 7.4 percent. According to Economy and Planning Minister Rodriguez, the average price of nickel, which represented 58 percent of all export revenue in 2007, dropped from USD 37,216 per ton to USD 21,837 as of November 2008. The price continued to drop into 2009 and currently floats between USD 11,000 and 12,000 per ton. Cuba produced 70,400 tons of nickel in 2008, down from 76,000 in 2007. The lower production was likely due to damage and delays caused by three major hurricanes. The GOC estimates that revenue from nickel exports was USD 250 million less than forecast for 2008. Regardless of the forecast, we estimate that nickel revenue was more than USD 1 billion less in 2008 than the record revenue earned in 2007. More than half of the nickel production is through a joint venture with Sherritt International of Canada.

¶9. (C) Nevertheless, the official press reported on January 5 that the nickel industry "gained economic leadership" over the tourism industry with USD 552 million in profit. The GOC has not reported its profit from tourism, but did report that the number of visitors in 2008 climbed by 9.3 percent and the corresponding revenue increased by 13.5 percent to USD 2.5 billion. A closer look at the data published shows that Canadian visitors continue to dominate the Cuban tourism industry. Through November, visitors from Canada represented one-third of all visitors in 2008 and over 75 percent of the increase in visitors. Visitors from Russia rose by 40 percent and from Poland by 100 percent, but their impact is significantly smaller than Canada and Western Europe. Visitors from all Western European countries were actually down in 2008. Return rates to Cuba are relatively low, and we understand that travel agencies are pushing hard for foreigners to visit Cuba now before the GOC or USG implements significant reforms.

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#### INFLATION AND UNEMPLOYMENT

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¶10. (SBU) GOC official statistics reported a December to December increase in the consumer price index of only 0.8 percent. This extremely low rate is notable not only because it is significantly lower than the 2007 rate of 2.8 percent and the 2006 rate of 5.7 percent, but also because 2008 saw the first increase in gas prices since 2005 (ref B). On September 8, regular gas prices rose by 69 percent and diesel by 87 percent. The GOC, holding true to their promise, revised gas prices again three months later, this time down by an average of 25 percent. Nevertheless, prices remain between 25 and 40 percent higher than before September, which trickles into all facets of the economy. In addition to higher fuel prices, the money supply grew by 9.4 percent, average wages grew by 1.5 percent (from CUP 408 per month to CUP 414, or about three more dollars per year), and prices for a variety of everyday purchases like soap, beer, and transportation went up. The reported 3.4 percent increase in the average consumer price index for 2008 and 2.6 percent higher GDP deflator used to calculate real GDP are more realistic inflation indicators, but most likely still on the low side.

¶11. (SBU) The official unemployment rate fell to a new historic low of 1.6 percent, or 79,600 people. The economically active population of 5 million men and women represents 69 percent of the population age 15 to 59. The remaining 31 percent, or 2.2 million people, are categorized as not actively looking for work but many of whom work in the informal economy. The agricultural sector employees nearly 20 percent of the workforce, and together with construction (18 percent), education (15 percent), and the very broad public health/social assistance/sport/tourism sector (13 percent) employs two-thirds of all active Cubans.

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## FISCAL DEFICIT

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¶12. (SBU) Similar to GDP, Cuban budget calculations mix both currencies and are therefore better analyzed in terms of changes than in absolute terms. Although revenues were 5.6 percent higher than budgeted (and 14.4 percent higher than 2007), the GOC outspent their budget by 9 percent (15.7 percent higher than 2007). Almost all of the higher spending went to food subsidies, fuel subsidies, and spending on housing and construction material post-hurricanes. Overall, the fiscal deficit grew by 63 percent to 6.7 percent of GDP. The 2009 budget plans to cut the fiscal deficit to 5.6 percent of GDP. As part of the budget, the GOC projects that subsidies will decrease slightly with lower international food and fuel prices.

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## RAUL'S SOLUTIONS AND COMMENTS

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¶13. (C) As noted in Ref A, Raul Castro offered few concrete remedies in response to Cuba's disappointing economic performance in 2008. In fact, he predicted an even more difficult environment in 2009 as a result of the world financial crisis. He said, "next year will be one of great uncertainty in the world economy and we should be prepared to take up that serious challenge which has been affecting us considerably." He discussed in general terms the need to adjust foreign currency spending to levels equivalent to foreign currency revenues by continued import substitution and increasing tourism and healthcare services. He also admonished "most people" for not properly valuing the services they receive for free as part of their compensation, but rather focusing on their monetary salary. He appeared to reference removing some of these subsidies and adjusting salaries accordingly. Castro exempted healthcare, education, and social security/assistance, which only leaves the ration card (food basket) and transportation as likely targets. In this same context he seemed to redefine socialism by stating that Cuba should "apply the socialist principle of everyone being compensated according to their work."

¶14. (C) Once again, Raul Castro has done well to identify some of Cuba's biggest economic problems, but any real solutions remain elusive or off target. His only concrete measures discussed in his National Assembly speech were cutting official travel by 50 percent and eliminating perks to government employees. He indicated that a proposal to establish a General Comptroller office will be discussed at the next National Assembly. Regarding any more substantial reforms, Castro promised that "these issues (subsidies and salaries) are very closely linked to the structural and conceptual transformation that shall be submitted to discussion to and approval by the Sixth (Communist) Party Congress." The much delayed Party Congress is scheduled for sometime in late 2009.

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